

NOTES TO FINANCIAL STATEMENTS

December 31, 2004

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

In June 1999, GASB unanimously approved Statement No. 34 "Basic Financial Statements and Management Discussion and Analysis for State and Local Governments." Significant changes in the Statement included the following:

- A Management Discussion and Analysis of the County's Overall position and results from operation.
- Financial statements prepared using full accrual accounting for all of the County's activities, including infrastructure (roads, bridges, etc.)
- A change in the fund financial statements focusing on the major funds.

These and other changes are reflected in the accompanying financial statements (including notes to the financial statements). The County has elected to implement the general provisions of the Statement in the current year and plans to retroactively report infrastructure (assets acquired prior to January 1, 2003) in the following years.

The financial statements of the County have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principals. The significant accounting policies are described below.

A. Reporting Entity

Lewis County was created on December 19, 1845, under the control of the Provisional Government of Oregon and operates under the laws of the State of Washington applicable to a Third Class County. The financial statements of Lewis County have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to local governmental units.

Lewis County is a general purpose government and provides the following services according to the Constitution and laws of the State of Washington: public safety, road improvement, parks and recreation, judicial administration, health and social services, senior services, and general administrative services.

Lewis County is governed by an elected board of three county commissioners. These financial statements include the financial position and results of operations for all fund types and its component units. Blended component units, although legally separate entities are, in substance, part of the County's operations and so data from these units are combined with data of the primary government. Each blended component unit has a December 31 year-end.

Blended Component Units

The Solid Waste Disposal District No. 1 of Lewis County is a quasi-municipal corporation, and an independent taxing authority and district, which is responsible for implementation of a comprehensive solid waste management plan for the County and other incorporated cities and towns within the county. In order to implement the plan and related goals, the County and the incorporated cities and towns within the county have agreed, through an interlocal agreement to the formation of the District and transfer of certain responsibilities to the District. Among obligations transferred to the District is the obligation to make funds available to the Centralia Landfill Closure Group for the closure, post-closure and remediation activities at the Centralia Landfill (which is operated by the City of Centralia). The District has the authority to provide for disposal of solid wastes within the boundaries of Lewis County. The District is governed by a three-member board, which consists of the three county commissioners. The District is reported as an enterprise fund.

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B. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the nonfiduciary activities of the primary government (and its component units). For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. (Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable.)

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Our policy is not to allocate indirect costs to a specific function or segment. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contribution that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

Separate fund financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the County considers revenues to be available if they are collected within a reasonable amount of time after the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, licenses, and interest associated within the current period are all considered to be susceptible to accrual and so have been recognized as revenues of the current period. Only the portion of special assessment receivable due within the current fiscal period is considered to be susceptible to accrual as revenue of the current period.

The County reports the following major governmental funds:

The Current Expense fund is the County's operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The Road Fund accounts for the design, construction and maintenance of county roads.

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The Capital Facilities Plan Fund is used to account for the 1/4 of 1% real estate excise tax to be used to finance capital projects including debt service for the Capital Facilities Plan.

The Community Development Block Grant (CDBG) Fund was used as a pass through fund for the 2004 CDBG to fund part of the Cardinal Glass plant.

The County reports the following major proprietary fund:

The Solid Waste Disposal District Fund is used to account for activity of Lewis County Solid Waste Disposal District No.1 and operation of the new solid waste transfer station in Southwest Centralia.

Additionally, the County reports the following fund types:

GOVERNMENTAL FUNDS - All governmental funds are presented using the flow of current financial resources measurement focus. This means that only current assets and current liabilities are generally included on their balance sheets. Their reported fund balance (net current assets) is considered a measure of "available expendable resources." Governmental fund operating statements focus on measuring changes in financial position, rather than net income; they present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets. The unreserved fund balance is a measure of available spendable resources.

General (Current Expense) Fund - This fund is the general operating fund of the county. It accounts for all financial resources and transactions except those required to be accounted for in another fund.

Special Revenue Funds - These funds account for revenues derived from specific taxes, grants, or other sources that are designated to finance particular activities of the county.

Debt Service Funds - These funds accounts for the accumulation of resources to pay principal, interest and related costs on general long-term debt.

Capital Project Funds - These funds account for the financial resources that are designated for the acquisition or construction of general governmental capital improvements.

PROPRIETARY FUNDS - Proprietary funds are accounted for on a cost of services or "capital maintenance" measurement focus. This means that all assets and all liabilities (whether current or non-current) associated with their activity are included on their balance sheets. Proprietary fund operating statements present increases (revenues and gains) and decreases (expenses and losses) in net total assets. Proprietary funds disclose changes in cash and cash equivalents by a separate statement that presents their cash flow, investing and financing activities. The government does not consistently apply all applicable FASB pronouncements issued after November 30, 1989 in accounting and reporting for its proprietary operations.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations.

Enterprise Funds - These funds account for operations that provide goods or services to the general public and are supported partially through user charges and primarily through property tax diversion.

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Internal Service Funds - These funds account for operations that provide goods or services to other departments or funds of the county or to other governmental units on a cost-reimbursement basis which include equipment rental, risk management, pits and quarries, facilities, county insurance and information services.

FIDUCIARY FUNDS - Fiduciary funds account for assets held by the county on behalf of other governments and other funds.

Agency Funds - These funds are custodial in nature (assets equal liabilities) and do not involve the measurement of results of operations.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The County has elected not to follow subsequent private-sector guidance.

As a general rule the effect of the interfund activity has been eliminated from the government-wide financial statements.

When both restricted and unrestricted resources are available for use, it is the County's policy to use unrestricted resources first, then restricted resources as needed.

Since the governmental fund statements are presented on a different measurement focus and basis of accounting than the government-wide statements' governmental column, a reconciliation is presented at the end of the statement, which briefly explains the adjustment necessary to transform the fund statements into the governmental-wide presentation.

D. Budgetary Information

1. **Budgets and Budgetary Accounting** - Annual budgets are adopted by the County's legislative authority at the fund level, except in the general fund, where expenditures may not exceed appropriations at the department level and the budgets constitute the legal authority for expenditures at that level.

Subsidiary revenue and expenditure ledgers are used to compare the budgeted amounts with actual revenues and expenditures. As a management control device, the subsidiary ledgers monitor expenditures for individual functions and activities by object class.

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for all governmental funds. All annual appropriations lapse at fiscal year end.

The financial statements do not present budgetary comparisons for proprietary fund types; however, annual budgets are adopted.

2. **Procedures for Adopting the Original Budget** - The County's budget procedures are mandated by RCW 36.40. The steps in the budget process are as follows:
 - a. Prior to the first Tuesday in September, the county commissioners' budget officer submits a proposed budget to the county commission. This budget is based on priorities established by the commission and estimates provided by county departments during the preceding months, and balanced with revenue estimates made by the departments, county commissioners' budget officer, and county treasurer.

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- b. The commission conducts public hearings on the proposed budget in October and December.
 - c. The commission makes adjustments to the proposed budget and adopts by resolution a final balanced budget no later than five days following the first Monday in December.
 - d. Within 30 days of adoption, the final budget is normally available to the public.
3. Amending the Budget - The budget, as adopted, constitutes the legal authority for expenditures. Budgets are reported according to Generally Accepted Accounting Principles (GAAP). Any revisions that alter the total expenditures of a fund or that affect the number of authorized employee positions, salary ranges, hours, or other conditions of employment must be approved by the county commission.

When the county commission determines that it is in the best interest of the county to increase or decrease the appropriation for a particular fund or department, it may do so by resolution approved by a simple majority after holding one public hearing.

The county's budget was amended 30 times during 2004, resulting in an increase to the budgets of the following funds:

| Fund | Times Amended | Total Budget |
|-------------------------|---------------|--------------|
| | | Change |
| General | 6 | \$655,313 |
| Social Services | 2 | 254,628 |
| SWW Fair | 1 | 50,000 |
| Communications | 2 | 245,877 |
| Community Development | 2 | 68,400 |
| Flood Control Zone | 1 | 271,314 |
| Paths and Trails | 1 | 13,000 |
| CDBG | 1 | 8,400,000 |
| Sheriff's Airplane | 1 | 1,500 |
| Public Health | 2 | 34,967 |
| Senior Transportation | 2 | 9,950 |
| SWW Fair Cum Reserve | 1 | 4,776 |
| Senior Services | 2 | 101,990 |
| South County Airport | 2 | 49,000 |
| Solid Waste Disp. Dist. | 1 | 291,865 |
| ER&R | 1 | 310,961 |
| Pits & Quarries | 1 | 50,000 |
| Risk Management | 1 | 300,000 |
| Facilities | 1 | 31,000 |
| Information Services | 1 | 1,110,795 |

The budget amounts shown in the financial statements are the final authorized amounts as revised during the year.

4. *Encumbrances* - The County does not employ encumbrance accounting.

E. Assets, Liabilities and Equities

1. *Cash and Cash Equivalents* - The county pools cash resources of its various funds in order to facilitate the management of cash. Income on pooled investments is allocated pursuant to county resolution no. 85-95. Cash applicable to a particular fund is readily identifiable. The balance in the pooled cash accounts is available to meet current operating requirements. Cash in excess of current requirements is invested in various interest-bearing securities and summarized by fund type in the combined balance sheet.

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The amounts reported as cash and equivalents also include compensating balances maintained with certain banks in lieu of payments for services rendered. The average compensating balances maintained during 2004 were approximately \$2,132,583.

The county's deposits are entirely covered by federal depository insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC).

For purposes of the statement of cash flows, the proprietary fund types considers all highly liquid investments including restricted assets with a maturity of three months or less when purchased to be cash equivalents, except for certificates of deposit and deposits with fiscal agents.

2. *Temporary Investments* - See Note 3.

3. *Receivables* - Taxes receivable consist of property taxes. See Note 4.

Accrued interest receivable consists of amounts earned on investments, notes and contracts at the end of the year.

Special assessments are recorded when levied. Special assessments receivable consists of current and delinquent assessments.

Customer accounts receivable consist of amounts owed from private individuals or organizations for goods and services including amounts owed for which billings have not been prepared.

Notes and contracts receivables consist of amounts owed on open accounts from private individuals or organizations for goods and services rendered.

4. *Amounts Due to and from Other Funds: Interfund Loans and Advances Receivable* - These accounts include all interfund receivables and payables. A separate schedule of interfund loans receivable and payable is furnished in Note 13.

5. *Amounts Due to and from Other Governmental Units* - These accounts include amounts due to or from other governments for grants, entitlement, temporary loans, taxes and charges for services.

6. *Inventories* - Inventories in governmental funds, under the FIFO method, consist of supplies held for consumption. The cost is recorded as expenditure at the time individual inventory items are consumed.

Inventories in proprietary funds are valued at cost by the weighted average method. The average cost is recorded as an expense at the time items are consumed.

7. *Restricted Assets and Liabilities* - These accounts contain resources for self-insurance programs held in internal service funds. Specific debt service reserve requirements are described in Long-Term Debt Note 11. In the Internal Service funds, restricted cash and investments at year-end were:

| Fund | Cash | Investments |
|------------------|------|--------------|
| Risk Management | - | \$ 4,745,196 |
| County Insurance | - | 686,823 |

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8. *Capital Assets and Depreciation* - Also See Note 6, Capital Assets. Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, and similar items), are reported in the applicable governmental or business-type columns in the government-wide financial statements. Capital assets are defined by the County as assets with an initial, individual cost of more than \$5,000 for non-infrastructure and \$50,000 for infrastructure. Such assets are recorded at estimated fair market value at the date of donation. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Property, plant, and equipment of the primary government is depreciated using the straight-line method over the following estimated useful lives:

| <u>Assets</u> | <u>Years</u> |
|------------------------------------|--------------|
| Autos, Computers, Office Equipment | 3 - 7 |
| Heavy Equipment | 8 -20 |
| Buildings, Land Improvements | 40 |
| Infrastructure | 15 - 60 |

9. *Other Property and Investments* - See Note 3, Investment.
10. *Other Assets and Debts* - These accounts reflect future resources needed to retire general long-term debt principal and amounts currently available in debt service or other funds to retire general long-term debt.
11. *Custodial Accounts* - This account reflects the liability for net monetary assets being held by the county in its trustee or agency capacity.
12. *Accumulated Unpaid Employee Leave Benefit* - The County records all accumulated unused vacation and sick leave benefits. Vacation pay which may accumulate up to 240 hours, is payable upon resignation, retirement or death. Sick leave may accumulate up to 1,320 hours. Fifty percent of outstanding sick leave to a maximum of 360 hours is payable upon resignation, retirement or death. For governmental funds, as of December 31, 2004 unused vacation and sick leave benefits of \$1,325,614 and \$1,451,664, respectively, including immaterial current portions, were recorded in the Government-wide Statement of Net Assets. In proprietary funds, the liability for unused vacation and sick leave benefits of \$184,168 and \$161,862 respectively, was expensed and recorded at December 31, 2004.
13. *Long-Term Debt* - See Note 11
14. *Deferred Revenues* - This account includes amounts recognized as receivables but not revenues in governmental funds because the revenue recognition criteria have not been met. (See note 1-F).
15. *Fund Balance Designations and Reservations* - In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

General Fund - The "Designated for Other Purposes" amount of \$1.5 million is a rainy day fund set aside by management.

16. *Net Assets* - See Note 14

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F. Revenues, Expenditures and Expenses

Under the modified-accrual basis of accounting:

1. Charges for services, interest on investments, and rents are generally considered measurable and available when earned in governmental funds.
2. Taxes and federal or state entitlement or shared revenues that have been collected but not remitted by an intermediary collection agency to the county are considered measurable and available.
3. Special assessments are considered measurable and available when they become current.
4. Grants are considered measurable and available to the extent that expenditures have been made. Other intergovernmental revenues are considered measurable and available when earned.
5. Interfund revenues for goods and services are considered measurable and available when earned.
6. Proceeds from refunded debt are recognized as an other financing source and the amount remitted to the refunding trustee is recognized as an other financing use (payment out of proceeds of refunding bonds) and expenditures (payments from other sources).
7. Proceeds from the sale or loss of capital assets are recognized as an other financing source.
8. Revenues from taxpayer-assessed taxes (e.g., sales tax), net of estimated refunds, are recognized when measurable and available to finance expenditures of the current period.
9. All other revenues are either not measurable or considered not available until collected.
10. Expenditures are generally recognized when incurred. (See note 1-C.)

Under the full accrual basis of accounting:

1. Revenues are recognized when earned, if measurable, and expenses are recognized when incurred, if measurable.

G. Non-Monetary Transactions

During the year, the internal service funds acquired capital assets valued at a cost of \$484,915, which did not require cash outflows. Those asset types are the result of contributions by other funds, and no gain or loss was recognized on the transfer.

H. Reclassification

There have been no reclassifications of 2003 balances.

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NOTE 2 - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

There have been no material violations of finance-related legal or contractual provisions, in any of the funds of the county.

NOTE 3 - INVESTMENTS AND DEPOSITS

A. Investments

As required by state law, all investments of the county's funds (except as noted below) are obligations of the US Government, the Washington State Treasurer's Investment Pool, the Washington State Committee for Deferred Compensation, bankers' acceptances, or deposits with Washington State banks and savings and loan institutions.

The county's investments are categorized into these three categories of credit risk:

1. Insured or registered, with securities held by the county or its agent in the county's name.
2. Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the county's name.
3. Uninsured and unregistered, with securities held by the counterparty or by its trust department or agent but not in the county's name.

Categories 2 and 3 do not apply to Lewis County.

All investments held at December 31, 2004, and throughout the year were classified as Category 1. There was no repurchase agreement activity during the year or outstanding as of December 31, 2004.

All temporary investments are stated at cost plus accrued interest, net of amortized premium or discount. Fair values are provided through a third party. The market pricing interfaces with our investment software and the prices are electronically updated. Other property and investments are shown on the combined balance sheet at cost, net of amortized premium or discount.

Management intends to hold the time deposits and securities until maturity. In accordance with generally accepted accounting principles applicable to regulated industries, reductions in market value are not reflected on the financial statements.

GASB statement 31 requires adjustments be made to the financial statements to reflect the difference between amortized cost and fair value of investments. At December 31, 2004, the difference between amortized cost and fair value due to economic market factors was not material. No adjustments have therefore been made.

Gains or losses on investments sold or exchanged are recognized at the time the transactions are completed.

The State Treasurer's Investment Pool is operated utilizing Rule 2a-7 like funds. Further, GASB 31 allows governmental entities utilizing Rule 2a-7 like funds to report the market value of their funds at amortized cost. As a governmental entity operated pool, there is no current SEC registration requirement. However, there is a State Treasurer's Investment Pool Advisory Committee, comprised of 12 persons, which provides oversight for the pool.

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B. Deposits

Certificates of deposits are entirely covered by federal depository insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC).

| | Category 1 | Carrying Amt. | Fair Value | Over/Under Carrying Amt. |
|---|----------------------|----------------------|----------------------|-----------------------------|
| A. Investments | | | | |
| US Gov't Securities | \$ 32,530,238 | \$ 32,530,238 | \$ 32,308,294 | \$ (221,944) |
| Municipal Bonds | 1,809,620 | 1,809,620 | 1,803,750 | (5,870) |
| Subtotal | 34,339,858 | 34,339,858 | 34,112,044 | (227,814) |
| <i>Investments Not Subject to Categorization:</i> | | | | |
| Investment in State Treasurer's Investment Pool | - | 47,128,337 | 47,128,337 | - |
| Total Investments | 34,339,858 | 81,468,195 | 81,240,381 | (227,814) |
| B. Deposits | | | | |
| Certificate of Deposit | 780,000 | 780,000 | 780,000 | - |
| Total Deposits | 780,000 | 780,000 | 780,000 | - |
| Total Investments and Deposits | \$ 35,119,858 | \$ 82,248,195 | \$ 82,020,381 | \$ (227,814) |

Proprietary fund restricted investments shown on the government-wide statement of net assets include the following:

| | Category 1 | Carrying Amount | Market Value |
|--|---------------------|---------------------|---------------------|
| US Gov't Securities | \$ 3,635,370 | \$ 3,635,370 | \$ 3,605,384 |
| Certificate of Deposits | 1,194,392 | 1,194,392 | 1,194,932 |
| <i>Investments Not Subject to Categorization:</i> | | | |
| Investment in State Treasurer's Investment Pool | | 602,257 | 602,257 |
| Total Investments and Deposits of Restricted Assets | \$ 4,829,762 | \$ 5,432,019 | \$ 5,402,573 |

Restricted cash in proprietary funds and deposits with fiscal agents shown on the government-wide statement of net assets include the following:

| | Category 1 | Carrying Amount | Bank Balance |
|---|-------------------|-------------------|-------------------|
| Insured (FDIC) | \$ 206,599 | \$ 206,599 | \$ 206,599 |
| Uninsured, collateralized by bank assets | 149,989 | 149,989 | 149,989 |
| Total Investments of Restricted Assets | \$ 356,588 | \$ 356,588 | \$ 356,588 |

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NOTE 4 - PROPERTY TAXES

The county treasurer acts as an agent to collect property taxes levied in the county for all taxing authorities. Collections are distributed as collected and those collections requiring remittance are distributed to other jurisdictions after the end of each month.

Property Tax Calendar

| | |
|-------------|--|
| January 1 | Taxes are levied and become an enforceable lien against properties. |
| February 14 | Tax bills are mailed. |
| April 30 | First of two equal installment payments is due. |
| May 31 | Assessed value of property is established for next year's levy at 100 percent of market value. |
| October 31 | Second installment is due. |

Property taxes are recorded as receivable when levied, offset by deferred revenue. During the year, property tax revenues are recognized when collected. No allowance for uncollectable taxes is established because delinquent taxes are considered fully collectible.

The county may levy up to \$1.80 per \$1,000 of assessed valuation for general governmental services, subject to the following two limitations stated in a and b:

- a. Washington State law in RCW 84.55 limits the growth of regular property taxes to an inflation limit factor percent per year, after adjustments for new construction. If the assessed valuation increases by more than the limit factor percent due to revaluation, the levy rate will be decreased. Additionally, upon a finding of 'substantial need' the legislative authority of taxing district other than the state may provide for the use of a limit factor of 106% or less.
- b. The Washington State Constitution limits the total regular property taxes to 1 percent of assessed valuation or \$10 per \$1,000 of value. If the taxes of all districts exceed this amount, each is proportionately reduced until the total is at or below the one percent limit.

The county is also authorized to levy \$2.25 per \$1,000 of assessed valuation in unincorporated areas for road construction and maintenance. This levy is subject to the same limitations as the levy for general governmental services. The county road levy for 2004 was \$2.0856 per \$1,000 on an assessed valuation of \$3,588,916,582 for a total road tax of \$7,485,175.

The county's total regular levy for 2004 was \$1.6035 per \$1,000 on an assessed valuation of \$4,948,453,878 for a total regular tax of \$7,935,000. The components of the regular levy are:

| | Levy | Tax |
|-----------------|--------|--------------|
| General Fund | 1.5671 | \$ 7,754,852 |
| Veterans Relief | 0.0113 | 55,908 |
| Mental Health | 0.0251 | 124,240 |
| Totals | 1.6035 | \$ 7,935,000 |

NOTE 5 - INTERGOVERNMENTAL GRANTS AND ENTITLEMENT

The accompanying Schedules of Financial Assistance provide a listing of all federal, state, and entitlement assistance programs in which the county participates

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NOTE 6 - CAPITAL ASSETS

Capital assets activity for the year ended December 31, 2004 was as follows:

| GOVERNMENTAL TYPE ACTIVITIES | Beginning Balance 1/1/2004 | Increases | Decreases | Ending Balance 12/31/2004 |
|--|---|------------------|------------------|--|
| Capital Assets, not being depreciated: | | | | |
| Land | \$ 2,052,678 | \$ 88,675 | \$ - | \$ 2,141,353 |
| Construction in Progress | 18,713,163 | 13,527,830 | 431,201 | 31,809,792 |
| Total Capital Assets, not being depreciated | 20,765,841 | 13,616,505 | 431,201 | 33,951,145 |
| Capital Assets being depreciated: | | | | |
| Buildings | 27,971,328 | 431,201 | - | 28,402,529 |
| Improvements other than buildings | 2,266,116 | - | - | 2,266,116 |
| Machinery & Equipment | 16,747,083 | 1,445,942 | 1,496,210 | 16,696,815 |
| Infrastructure | 6,361,941 | 1,099,054 | - | 7,460,995 |
| Total Capital Assets, being depreciated | 53,346,468 | 2,976,197 | 1,496,210 | 54,826,455 |
| Less Accumulated Depreciation for: | | | | |
| Buildings | 19,262,628 | 358,316 | - | 19,620,944 |
| Improvements other than buildings | 1,328,409 | 97,863 | - | 1,426,272 |
| Machinery & Equipment | 11,293,308 | 1,167,504 | 1,200,175 | 11,260,637 |
| Infrastructure | 277,958 | 332,911 | - | 610,869 |
| Total Accumulated Depreciation | 32,162,303 | 1,956,594 | 1,200,175 | 32,918,722 |
| Total Capital Assets being depreciated, net | 21,184,165 | 1,019,603 | 296,035 | 21,907,733 |
| Governmental Type Activities Capital Assets, net | \$ 41,950,006 | \$ 14,636,108 | \$ 727,236 | \$ 55,858,878 |

Depreciation Expense was charged to functions as follows:

| | |
|---------------------------------|-------------------|
| General Government Services | \$ 359,700 |
| Security of Person and Property | 56,877 |
| Physical Environment | 3,007 |
| Transportation | 345,894 |
| Economic Environment | 2,282 |
| Mental and Physical Health | 2,424 |
| Culture and Recreation | 3,883 |
| | <u>\$ 774,067</u> |

In addition, depreciation on capital assets held by
by the County's internal service funds is charged
to the various functions based upon their usage of
the assets.

1,162,084

Total Governmental Activities Depreciation Expense

\$ 1,936,151

NOTES TO FINANCIAL STATEMENTS

December 31, 2004

| BUSINESS TYPE ACTIVITIES | Beginning Balance 1/1/2004 | Increases | Decreases | Ending Balance 12/31/2004 |
|--|----------------------------------|-------------|-----------|---------------------------------|
| Capital Assets, not being depreciated: | | | | |
| Land | \$ 100,653 | \$ - | \$ - | \$ 100,653 |
| Construction in Progress | 1,399,232 | 5,375 | - | 1,404,607 |
| Total Capital Assets, not being depreciated | 1,499,885 | 5,375 | - | 1,505,260 |
| Capital Assets being depreciated: | | | | |
| Buildings | 1,126,367 | 54,180 | - | 1,180,547 |
| Improvements other than buildings | 506,453 | - | - | 506,453 |
| Machinery & Equipment | 355,631 | - | - | 355,631 |
| Total Capital Assets, being depreciated | 1,988,451 | 54,180 | - | 2,042,631 |
| Less Accumulated Depreciation for: | | | | |
| Buildings | 614,121 | 45,823 | - | 659,944 |
| Improvements other than buildings | 246,770 | 19,039 | - | 265,809 |
| Machinery & Equipment | 67,530 | 23,345 | - | 90,875 |
| Total Accumulated Depreciation | 928,421 | 88,207 | - | 1,016,628 |
| Total Capital Assets being depreciated, net | 1,060,030 | (34,027) | - | 1,026,003 |
| Business Type Activities Capital Assets, net | \$ 2,559,915 | \$ (28,652) | \$ - | \$ 2,531,263 |

Depreciation Expense was charged to functions as follows:

| | |
|-------------|------------------|
| Solid Waste | \$ 75,528 |
| Airport | 12,679 |
| Total | <u>\$ 88,207</u> |

NOTES TO FINANCIAL STATEMENTS

December 31, 2004

NOTE 7 - PENSION PLANS

Substantially all county full-time and qualifying part-time employees participate in one of the following statewide local government retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing multiple-employer defined benefit public employee retirement plans and defined contribution retirement plans.

The Department of Retirement Systems (DRS), a department within the primary government of the State of Washington, issues a publicly available comprehensive annual financial report (CAFR) that includes financial statements and required supplementary information for each plan. The DRS CAFR may be obtained by writing to:

Department of Retirement Systems
Communications Unit
PO Box 48380
Olympia, WA 98504-8380

A. Public Employees' Retirement System (PERS) Plans 1, 2 and 3

Plan Description: PERS is a cost-sharing multiple-employer retirement system comprised of three separate plans for membership purposes: Plans 1 and 2 are defined benefit plans and Plan 3 is a combination defined benefit/defined contribution plan. Membership in the system includes: elected officials; state employees; employees of the Supreme, Appeals, and Superior courts (other than judges in a judicial retirement system); employees of legislative committees; community and technical colleges, college and university employees (not in national higher education retirement programs); judges of district and municipal courts; and employees of local governments. PERS participants who joined the system by September 30, 1977, are Plan 1 members. Those who joined on or after October 1, 1977 and by either, February 28, 2002 for state and higher education employees, or August 31, 2002 for local government employees, are Plan 2 members unless they exercise an option to transfer their membership to Plan 3. PERS participants joining the system on or after March 1, 2002 for state and higher education employees, or September 1, 2002 for local government employees have the option of choosing membership in either PERS Plan 2 or PERS Plan 3. The option must be exercised within 90 days of employment. An employee is reported in Plan 2 until a choice is made. Employees who fail to choose within 90 days default to PERS Plan 3. PERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. PERS retirement benefit provisions are established in state statute and may be amended only by the State Legislature.

Plan 1 retirement benefits are vested after an employee completes five years of eligible service. Plan 1 members are eligible for retirement at any age after 30 years of service, or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. The annual pension is 2 percent of the average final compensation per year of service, capped at 60 percent. The average final compensation is based on the greatest compensation during any 24 eligible consecutive compensation months. If qualified, after reaching the age of 66 a cost-of-living allowance is granted based on years of service credit and is capped at 3 percent annually.

Plan 2 retirement benefits are vested after an employee completes five years of eligible service. Plan 2 members may retire at the age of 65 with five years of service, or at the age of 55 with 20 years of service, with an allowance of 2 percent of the average final compensation per year of service. The average final compensation is based on the greatest compensation during any eligible consecutive 60-month period. Plan 2 retirements prior to the age of 65 received reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. There is no cap on years of service credit; and a cost-of-living allowance is granted (indexed to the Seattle Consumer Price Index), capped at 3 percent annually.

NOTES TO FINANCIAL STATEMENTS

December 31, 2004

Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. The defined benefit provides a benefit calculated at 1 percent of the average final compensation per year of service. The average final compensation is based on the greatest compensation during any eligible consecutive 60-month period. Plan 3 members become eligible for retirement if they have: at least ten years of service; or five years including twelve months that were earned after age 54; or five service credit years earned in PERS Plan 2 prior to June 1, 2003. Plan 3 retirements prior to the age of 65 received reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. There is no cap on years of service credit; and Plan 3 provides the same cost-of-living allowance as Plan 2. The defined contribution portion can be distributed in accordance with an option selected by the member, either as a lump sum or pursuant to other options authorized by the Employee Retirement Benefits Board.

There are 1,168 participating employers in PERS. Membership in PERS consisted of the following as of the latest actuarial valuation date for the plans of September 30, 2003:

| | |
|--|----------------|
| Retirees & Beneficiaries Receiving Benefits | 65,362 |
| Terminated Plan Members Entitled To But Not Yet Receiving Benefits | 20,001 |
| Active Plan Member Vested | 100,469 |
| Active Plan Members Nonvested | 54,081 |
| Total | 239,913 |

Funding Policy: Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates, Plan 2 employer and employee contribution rates, and Plan 3 employer contribution rates. Employee contribution rates for Plan 1 are established by statute at 6 percent for state agencies and local government unit employees, and 7.5 percent for state government elected officials. The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. All employers are required to contribute at the level established by the Legislature. PERS Plan 3 defined contribution is a non-contributing plan for employers. Employees who participate in the defined contribution portion of PERS Plan 3 do not contribute to the defined benefit portion of PERS Plan 3. The Employee Retirement Benefits Board sets Plan 3 employee contribution rates. Six rate options are available ranging from 5 to 15 percent; two of the options are graduated rates dependent on the employee's age. The methods used to determine the contribution requirements are established under state statute in accordance with chapters 41.40 and 41.45 RCW.

The required contribution rates expressed as a percentage of covered payroll, as of December 31, 2004 were:

| | PERS Plan 1 | PERS Plan 2 | PERS Plan 3 |
|-----------|--------------------|--------------------|--------------------|
| Employer* | 1.38% | 1.38% | 1.38% |
| Employee | 6.00% | 1.18% | *** |

* The employer rates include the employer administrative expense fee currently set at 0.19%

**Plan 3 defined benefit portion only.

***Variable from 5.0% minimum to 15.0% maximum to based on rated selected by the PERS 3 member.

Both county and the employees made the required contributions. The county's required contributions for the years ended December 31, were:

| | PERS Plan 1 | PERS Plan 2 | PERS Plan 3 |
|------|--------------------|--------------------|--------------------|
| 2004 | \$ 34,414 | \$ 235,624 | \$ 18,738 |
| 2003 | 35,126 | 223,482 | 12,412 |
| 2002 | 37,657 | 237,524 | 657 |

NOTES TO FINANCIAL STATEMENTS

December 31, 2004

B. Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plans 1 and 2

Plan Description: LEOFF is a cost-sharing multiple-employer retirement system comprised of two separate defined benefit plans. Membership in the system includes all full-time, fully compensated, local law enforcement officers and firefighters. LEOFF is comprised primarily of non-state employees, with the exception of the Department of Fish and Wildlife enforcement officers, who were first included prospectively effective July 27, 2003. LEOFF participants who joined the system by September 30, 1977 are Plan I members. Those who joined on or after October 1, 1977 are Plan 2 members. Effective July 1, 2003, the LEOFF Plan 2 Retirement Board was established to provide governance of LEOFF Plan 2. The Board's duties include adopting contribution rates and recommending policy changes to the Legislature for the LEOFF Plan 2 retirement plan. Effective January 1, 2003 firefighter emergency medical technicians (EMTs) may transfer PERS Plan 1 or Plan 2 service credit to LEOFF Plan 2 if while employed for the city, town, county or district, the EMT's job was relocated to a fire department of another city, town, county or district. LEOFF defined benefits are financed from a combination of investment earnings, employer and employee contributions, and a special funding situation in which the state pays the remainder through state legislative appropriations. LEOFF retirement benefit provisions are established in state statute and may be amended only by the State Legislature.

Plan 1 retirement benefits are vested after an employee completes five years of eligible service. Plan 1 members are eligible for retirement with five years of service at the age of 50. The benefit per year of service calculated as a percent of final average salary is as follows:

| Term of Service | Percent of Final Average |
|-----------------|--------------------------|
| 20+ | 2.00% |
| 10-20 | 1.50% |
| 5-10 | 1.00% |

The final average salary is the basic monthly salary received at the time of retirement, provided a member has held the same position or rank for 12 months preceding the date of retirement. Otherwise, it is the average of the highest consecutive 24 months' salary within the last 10 years of service. If membership was established in LEOFF after February 18, 1974, the service retirement benefit is capped at 60 percent of final average salary. A cost-of-living allowance is granted (indexed to the Seattle Consumer Price Index).

Plan 2 retirement benefits are vested after an employee completes five years of eligible service. Plan 2 members may retire at the age of 50 with 20 years of service, or at the age of 53 with five years of service, with an allowance of 2 percent of the final average salary per year of service. The final average salary is based on the highest consecutive 60 months. Plan 2 retirements prior to the age of 53 are reduced 3 percent for each year that the benefit commences prior to age 53. There is no cap on years of service credit; and a cost-of-living allowance is granted (indexed to the Seattle Consumer Price Index), capped at 3 percent annually.

There are 368 participating employers in LEOFF. Membership in LEOFF consisted of the following as of the latest actuarial valuation date for the plans of September 30, 2003:

| | |
|--|---------------|
| Retirees & Beneficiaries Receiving Benefits | 8,370 |
| Terminated Plan Members Entitled to But Not Yet Receiving Benefits | 453 |
| Active Plan Members Vested | 11,548 |
| Active Plan Member Nonvested | 4,003 |
| Total | 24,374 |

NOTES TO FINANCIAL STATEMENTS

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Funding Policy: Starting on July 1, 2000, Plan 1 employers and employees will contribute zero percent as long as the plan remains fully funded. Employer and employee contribution rates are developed by the Office of the State Actuary to fully fund the plan. Plan 2 employers and employees are required to pay at the level adopted by the Department of Retirement Systems in accordance with 41.45 RCW. All employers are required to contribute at the level required by state law. The Legislature, by means of a special funding arrangements, appropriated money from the state General Fund to supplement the current service liability and fund the prior service costs of Plan 2 in accordance with the requirements of the Pension Funding Council. However, this special funding situation is not mandated by the state constitution and this funding requirement could be returned to the employers by a change of statute. The methods used to determine the contribution rates are established under state statute in accordance with chapters 41.26 and 41.45 RCW.

The required contribution rates expressed as a percentage of current year covered payroll, as of December 31, 2004 were:

| | LEOFF Plan 1 | LEOFF Plan 2 |
|-----------|---------------------|---------------------|
| Employer* | 0.19% | 3.25% |
| Employee | 0.00% | 5.09% |
| State | n/a | 2.03% |

* The employer rates do not include the administrative expense fee currently set at 0.19%.

**The employer rate for ports and university is 5.28%.

Both county and the employees made the required contributions. The county's required contributions for the years ended December 31, were:

| | LEOFF Plan 1 | LEOFF Plan 2 |
|------|---------------------|---------------------|
| 2004 | \$ 663 | \$ 70,061 |
| 2003 | 644 | 61,975 |
| 2002 | 708 | 52,441 |

NOTE 8 - POSTRETIREMENT HEALTH CARE BENEFITS

In accordance with the Washington Law Enforcement Officers and Fire Fighters Retirement System (LEOFF) Act (RCW 41.26), the county provides certain health care benefits for retired full-time, fully compensated, law enforcement officers who established membership in the LEOFF 1 retirement system on or before September 30, 1977. Substantially all of the county's law enforcement officers who established membership in the LEOFF 1 retirement system may become eligible for those benefits when they reach normal retirement age. The Lewis County Sheriff's Department, in conjunction with the Lewis County Disability Board, reimburses retired LEOFF 1 law enforcement officers for reasonable medical charges as described in the LEOFF act. In 2004, 19 retirees received benefits under this act. As of December 31, 2004, there were 5 active officers with an average age of 53 who become eligible for benefits when they reach normal retirement age.

The cost of retiree health care benefits is recognized as an expenditure in the General Fund as claims are incurred. For 2004, those costs totaled \$168,228, with an average cost per retiree of \$8,854.

During 1993 the county began setting aside funds for future post retirement health care benefit payments for the county's LEOFF 1 law enforcement officers. The net assets available at December 31, 2004 were \$4,745,196, shown as a restricted investment in the internal service fund, Risk Management; however, the current strategy does not constitute an advance-funded approach.

NOTES TO FINANCIAL STATEMENTS

December 31, 2004

NOTE 9 - DEFERRED COMPENSATION PLAN

The county offers its employees deferred compensation plans created in accordance with Internal Revenue code Section 457. Two plans are available, one with State of Washington Department of Retirement Systems, Deferred Compensation Program and a second with Public Employees Benefit Services Corporation (PEBSCO). The plans, available to all eligible employees, permit them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

Plan assets for both the State of Washington Deferred Compensation Program and PEBSCO plans reside in trust held for exclusive benefit of participants and their beneficiaries. Pursuant to Governmental Accounting Standards Board (GASB) Statement 32, since Lewis County is no longer the owner of these assets, as of December 31, 1998, the plan assets and liabilities are no longer reported as an Agency Fund.

NOTE 10 - RISK MANAGEMENT

Liability: Lewis County is a member of the Washington Counties Risk Pool. Chapter 48.62 RCW authorizes the governing body of any one or more governmental entities to form together into or join a pool or organization for the joint purchasing of insurance, and/or joint self-insuring, and/or joint hiring or contracting for risk management services to the same extent that they may individually purchase insurance, self-insure, or hire or contract for risk management or contract for risk management services. An agreement to form a pooling arrangement was made pursuant to the provisions of Chapter 39.34 RCW, the Interlocal Cooperation Act. The pool was formed on August 18, 1988 when counties in the State of Washington joined together by signing an Interlocal Agreement to pool their self-insured losses and jointly purchase insurance and administrative services. Twenty-eight counties have joined the pool. The pool allows members to establish a plan of self-insurance, jointly purchase excess or reinsurance and provide related services. All pool joint self-insurance liability coverage's, including public officials errors and omissions, are on an "occurrence" basis. The pool also provides special events/ concessionaires optional group insurance coverage for its members.

Members make an annual contribution to fund the pool. The pool acquires reinsurance from unrelated underwriters that are subject to a pool per-occurrence self-insured retention (SIR) of \$500,000. Members may elect deductible amounts ranging from \$5,000 per occurrence to \$250,000, and are responsible for the first deductible amounts of each claim, while the pool is responsible for the remaining difference up to the pool's \$500,000 SIR. Reinsurance carriers cover all losses over \$500,000 to the maximum limits of each policy. Since the pool is a cooperative program, there is a joint liability among the participating members.

Members contract to remain in the pool for a minimum of five years, and must give notice one year before terminating participation. The Interlocal Agreement is renewed automatically each year until terminated. Even after termination, a member is still responsible for contributions to the pool for any unresolved, unreported, and in-process claims for the period it was a signatory to the Interlocal Agreement.

The pool is fully funded by its member participants and claims are filed by the same. It is governed by a board of directors, which is comprised of one designated representative from each participating member. An executive committee is elected at the annual meeting, and is responsible for conducting the business affairs of the pool.

Lewis County's SIR is in effect for general liability losses up to \$25,000, \$100,000, or \$250,000, dependent on claim date, per occurrence, and those in excess of the retention are insured by the Washington Counties Risk Pool to \$10,000,000. As of December 31, 2004, settlements, if any, have not exceeded insurance coverage.

NOTES TO FINANCIAL STATEMENTS

December 31, 2004

The county maintains insurance against most normal hazards except for unemployment and worker's compensation, where it has elected to become partially self-insured.

Risk Management Fund: - The county established its own Risk Management fund in 1991, which is used to pay deductibles on general liability claims and unemployment claims. The county has elected to become self-insured for unemployment claims, and utilizes an independent claims management firm to review and process claims. Based on Washington Counties Risk Pool, unemployment claims management firm and county management estimates, the county's estimated liability for probable losses at December 31, 2004, which includes estimates for IBNR's (Incurred But Not Reported claims) were as follows:

| | 2003 | 2004 |
|--------------------------|---------------------|---------------------|
| General Liability Claims | \$ 1,000,000 | \$ 1,000,011 |
| Unemployment Claims | 114,602 | 99,370 |
| Total | \$ 1,114,602 | \$ 1,099,381 |

In addition, the following shows changes in the balances of claims liabilities during the past year:

| | Year Ended 12/31/2003 | Year Ended 12/31/2004 |
|--|--------------------------|--------------------------|
| Unpaid claims, beginning of fiscal year | \$ 1,145,418 | \$ 1,114,602 |
| Incurred claims & changes in estimate | 270,193 | 172,995 |
| Claim Payments | (301,009) | (188,216) |
| Unpaid claims, end of fiscal year | \$ 1,114,602 | \$ 1,099,381 |

As of December 31, 2004, cash and investments were \$2,899,791 and \$4,745,196 in unrestricted and restricted (LEOFF 1 post retirement assets), respectively, and net assets were \$6,763,385.

County Insurance Fund: - The county has elected to become self-insured for worker's compensation and maintains the County Insurance Fund which is used to pay related claims costs. An independent claims management firm processes claims. Based on the claims management firm's estimates and Washington State Department of Labor & Industries data, the county's estimated liability for probable losses at December 31, 2004 was \$671,133:

| | Year Ended 12/31/2003 | Year Ended 12/31/2004 |
|--|--------------------------|--------------------------|
| Unpaid claims, beginning of fiscal year | \$ 334,983 | \$ 334,983 |
| Incurred claims & changes in estimate | 201,539 | 191,892 |
| Claim Payments | (201,539) | (191,892) |
| Unpaid claims, end of fiscal year | \$ 334,983 | \$ 334,983 |

Additionally, the county has an assignment of account agreement with the Washington State Department of Labor and Industries for a single surviving spouse pension obligation. The pension obligation as calculated by the state is \$190,073 plus a three-month deposit of \$4,318. The county has a restricted certificate of deposit for \$190,073 to secure the pension, and the state holds the \$4,318 deposit. The county has met the SIR payable under the excess coverage for the specific claim.

The county is required by Washington State Department of Labor and Industries to set aside, for protection to the Workers' Compensation Fund, a minimum of \$100,000 in cash reserves. Additionally, the county has purchased \$1 million of excess coverage insurance for workers' compensation claims, with the county's aggregate SIR of \$500,000 for the current two-year policy period. The policy has a lower SIR for individual claims, which varies with each policy

NOTES TO FINANCIAL STATEMENTS

December 31, 2004

year. As of December 31, 2004, cash and investments were \$379,371 and \$686,823 in unrestricted and restricted assets, respectively and net assets were \$761,576.

Other Insurance: - The county has purchased coverage for property insurance (including computers), flood, auto and equipment physical damage, boiler, and liability for Packwood, Chehalis/Centralia, and South County Airports. For the past three fiscal years, there were no settlements that exceeded insurance coverage.

NOTE 11 - LONG-TERM DEBT

The County may issue general obligation and revenue bonds to finance the purchase of major capital items, the acquisition or construction of major capital facilities and other major items. The general obligation bonds have been issued for the general government and are being repaid from applicable resources. The County is also liable for notes that were entered into for various reasons stated below in the description of each note. These notes are considered obligations of the general government and are being repaid with general governmental revenue sources.

A. Disclosures About Each Significant Debt Incurred

| | Outstanding <u>12/31/2004</u> |
|---|----------------------------------|
| <u>General Obligation Bonds</u> | |
| \$12,270,000 - Issued February 26, 2003, for the purpose of constructing a new jail facility. Interest is paid at 3.00% to 4.75% with annual debt service payments of \$794,378 to \$838,000 through December 1, 2027. | \$11,560,000 |
| \$13,795,000 - Issued October 27, 1999, for the purpose of refunding the outstanding 1992 GO bonds and financing part of Phase 1 of the County's Comprehensive Capital Facilities Plan. The plan includes remodeling of current facilities, property acquisition and construction of new County buildings. Interest is paid at 4.50% to 6.25% with annual debt service payments of \$488,772 to \$1,068,813 through December 1, 2024. | 12,355,000 |
| <u>Notes Payable</u> | |
| <i>Washington State, Public Works Trust Fund Loan - Dept. of Community Development - \$389,125</i> - Issued April 14, 1994, for the purpose of financing extension of roads and utility services as an expansion of the Chehalis Industrial Park; whereby, the county acted as the lead agency in a cooperative project with the Port of Chehalis. All principal and interest payments made by the county are reimbursed 100% by the Port of Chehalis. Interest is paid at 1.00% on annual installments of \$23,083 to \$31,704 through July 1, 2014. | 277,946 |
| <i>Washington State Revolving Fund Loan - Dept. of Ecology - \$406,261</i> - Issued July 1, 1994, for the purpose of paying for costs associated with the Wallace Road sewer project. The loan agreement provides a maximum allowable loan of \$406,261, of which the County has received \$322,808. Interest is paid at 4.50% on semi annual installments of \$12,297 through July 1, 2014. | 188,421 |
| Total Outstanding Debt | <u>\$24,381,367</u> |

NOTES TO FINANCIAL STATEMENTS

December 31, 2004

B. Debt Service Requirements to Maturity

The annual requirements to amortize outstanding debt, including interest and capital lease payments, are as follows:

| Year Ended | G.O. Bonds | Notes | Total Debt |
|--|----------------------|-------------------|----------------------|
| 2005 | \$ 1,850,083 | \$ 55,168 | \$ 1,905,251 |
| 2006 | 1,848,033 | 54,890 | 1,902,923 |
| 2007 | 1,854,933 | 54,613 | 1,909,546 |
| 2008 | 1,855,383 | 54,334 | 1,909,717 |
| 2009 | 1,858,670 | 54,057 | 1,912,727 |
| 2010-2027 | 30,610,998 | 253,809 | 30,864,807 |
| TOTAL | \$ 39,878,100 | \$ 526,871 | \$ 40,404,971 |
| Less: Portion of Debt Representing Interest | 15,963,100 | 60,504 | 16,023,604 |
| Principal Payments | \$ 23,915,000 | \$ 466,367 | \$ 24,381,367 |

C. Changes in Government-wide Long-Term Debt

The following is a summary of the County's Long-Term Debt transactions for the year ended December 31, 2004:

| | Balance 12/31/2003 | New Issues | Retirement | Balance 12/31/2004 |
|--------------------------|-----------------------|---------------------|---------------------|-----------------------|
| Compensated Absences | \$ 2,988,171 | \$ 3,123,729 | \$ 2,988,171 | \$ 3,123,729 |
| General Obligation Bonds | 24,550,000 | - | 635,000 | 23,915,000 |
| Notes Payable | 509,749 | - | 43,382 | 466,367 |
| TOTAL | \$ 28,047,920 | \$ 3,123,729 | \$ 3,666,553 | \$ 27,505,096 |

D. Assets Available for Debt Service

At December 31, 2004, the county has \$1,176 available in the debt service funds. The general fund and other county funds will transfer assets as required to service the general obligation bonded debt. Other debt is serviced by assets within the benefiting fund.

E. Legal Debt Margin

State law sets the county's limitation on external long-term debt as follows:

| Purpose of Indebtedness | Remaining Capacity |
|-----------------------------------|--------------------|
| General Gov't (no vote required) | \$ 18,165,669 |
| General Gov't (3/5 majority vote) | \$ 116,335,702 |

F. Prior Years' Debt Defeasance

In prior years, the County defeased two bond issues by creating separate irrevocable trust funds. New debt has been issued and the proceeds used to purchase U.S. government securities that were placed in the trust funds. The investments and fixed earnings from the investments are sufficient to fully service the defeased debt until the debt is called or matures. For financial reporting purposes, the debt has been considered defeased and therefore removed as a liability from the County's government wide financial statements. As of December 31, 2004, the amount of defeased debt outstanding but removed from the Solid Waste Disposal District amounted to \$6,629,074 and the Governmental Long Term Debt amounted to \$0, as the underlying bonds were called in 2003.

NOTES TO FINANCIAL STATEMENTS

December 31, 2004

NOTE 12 - JUDGMENTS AND CONTINGENCIES

The county has recorded in its financial statements all material liabilities, including an estimate for situations, which are not yet resolved, but where, based on available information, management believes it is probable that the county will have to make payment. In the opinion of management, the county's insurance policies and/or self-insurance reserves are adequate to pay all known or pending claims.

The county participates in a number of federal and state assisted programs. These grants are subject to audit by the grantors or their representative. Such audits could result in requests for reimbursement to grantor agencies for expenditures disallowed under the terms of the grants. Management believes that such disallowances, if any, will be immaterial.

Landfill Closure: On August 28, 1990, the Centralia Landfill was listed on the Washington State Hazardous Sites List pursuant to Chapter 70, 105D RCW, the Model Toxics Control Act, and WAC 173-340-330, and on August 30, 1990, the Landfill was added to the Federal National Priorities List (NPL) pursuant to 42 U.S.C. Section 9605 of the Comprehensive Environment Response, Compensation, and Liability Act (CERCLA or Superfund). As a result of these listings, it was necessary for the Landfill to be remeditated pursuant to the requirements of these laws.

On May 1, 1990 an Interlocal agreement was made between the various municipalities within Lewis County forming the Centralia Landfill Closure Group (CLCG) regarding the closure of the Centralia landfill. The municipalities, by the agreement, commit to take all action reasonably necessary to comply with the Environmental Laws and to share the costs of such compliance. Lewis County's (unincorporated portion) potential liability represents 48.85% of the closure costs.

In addition to the municipalities, other PLPs (Potentially Liable Parties) and insurance carriers for the municipalities have been identified. The Washington State Department of Ecology (DOE) has evaluated information related to each PLP and found that credible evidence existed to notify two firms of their potential liability. Insurance carriers for the municipalities have been involved at various levels of the closure process, assisting in the duty to defend and to cover costs of the closure. As of December 1997, \$3,430,481 had been recovered from insurance carriers.

During 1993, Lewis County concluded the process of forming a countywide Solid Waste Disposal District. Reportable financial activity of the district began in the spring of 1994, then the district assumed the local government's share of the liability for the Centralia Landfill closure. The maximum liability to the Lewis County Solid Waste Disposal District as well as all signatory municipalities to the landfill closure interlocal agreement, is capped at \$13 million.

Also in 1994, the Lewis County Solid Waste Disposal District #1 forwarded the sum of \$8.7 million to the city of Centralia to fulfill the assumption of the local government's share of the liability for the Centralia Landfill closure. Therefore, the potential remaining obligation to the Disposal District as well as all signing municipalities is \$4.3 million with Lewis County either alone or through its Disposal District, responsible for 48.85% of that \$4.3 million (\$2.1 million). However, current estimates indicate that there may be no future costs to Lewis County; accordingly, no additional liabilities for closure have been recorded in the Lewis County Solid Waste Disposal District fund.

Since the closure project is currently included on the National Priorities List pursuant to the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA" and "Superfund"), there is potential financial assistance available through the State of Washington Department of Ecology for a percentage (historically 75%) of the closure costs. As of December 1997, the CLCG had received a total of \$7,909,813 from 1991 through 1997 in grant proceeds from the Department of Ecology. Current assessments indicate that future Ecology participation in closure activities will be in the area of 40% participation due to declining resources at the state level.

NOTES TO FINANCIAL STATEMENTS

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Interim action has been completed, pursuant to an initial consent decree, to provide a final cover over closed portions of the landfill. Completion of this project will reduce ultimate closure costs. The estimated total cost for the interim action was over \$9.6 million, with financial assistance from the Washington State DOE. Lewis County's share is represented by 48.85% of the local cost. The sale of the bonds in 1994 partially offset those costs.

Within the landfill closure account managed by the CLCG, there have been adequate resources (factoring the \$8.7 million forwarded to the CLCG by the Disposal District) to cover costs associated with remedial work undertaken thus far. The Solid Waste Disposal District transferred \$238,343 during the year and at the end of 2004, \$188,656 remained in the City of Centralia Landfill Operating Trust Account, administered by the CLCG.

Significant decreases in the fund were the result of expenditures for post closure mitigation and the return of \$8.7 million to Lewis County Solid Waste Disposal District #1. Increases to the landfill closure fund were the result of changes in known circumstances. The liability will continue to change as expenditures occur and as known circumstances occur due to the engineering determinations, inflation, deflation, technology or applicable laws or regulations and the completion of Remedial Investigation, Feasibility Study, and Closure Action Plan (RI/FS/CAP) negotiations with the Department of Ecology.

The CLCG, PLPs and insurance carriers have negotiated for the second consent decree with the Washington State DOE. A Remedial Investigation and Feasibility Study (RI/FS) has begun. Once completed, the results will be used to formulate the Closure Action Plan (CAP) which was completed in 2001. This plan will be approved by the DOE. It is possible that the landfill will be de-listed from CERCLA at the completion of the RI/FS because of pressure on the Environmental Protection Agency from the United States Congress, but that possibility is remote.

In April 1997, the Centralia Landfill Closure Group forwarded \$8.7 million to the Lewis County Solid Waste Disposal District, as these funds were no longer needed for landfill closure costs. On May 6, 1997, this money, along with other funds set aside in the Solid Waste Disposal District fund as debt service reserves, were utilized to defease the \$9,485,000 of the District's 1994 Revenue Bonds. The District acquired and deposited U.S. Government obligations irrevocably in escrow with First Trust National Association, Seattle, Washington, in amounts sufficient to pay the principal of and interest on the 1994 bonds through the final date of maturity, November 1, 2015. The payment of the debt service on the 1994 Bonds will be made solely from the U.S. Government Obligations and no longer constitutes a lien and charge on the revenues of the District.

The total costs to Lewis County Solid Waste Disposal District in the future, and the period of time over which such costs will be incurred are reasonably predictable at this time.

NOTE 13 - INTERFUND TRANSACTIONS AND BALANCES

A. Classification of Interfund Transactions

Interfund transactions are classified as follows:

1. Services Provided - Transactions that would be treated as revenues, expenditures or expenses if they involve external organizations, such as buying goods and services or payments in lieu of taxes, are similarly treated when they involve other funds of Lewis County.
2. Transfers - Transactions to support the operations of other funds are recorded as "Transfers" and classified with "Other Financing Sources or Uses" in the fund statements. Transfers between governmental or proprietary funds are netted as part of the reconciliation to the Government-wide financial statements.

NOTES TO FINANCIAL STATEMENTS

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3. Contributions - Contributions to the capital of enterprise or internal service funds, transfers of capital assets between proprietary and governmental funds, transfers to establish or reduce working capital in other funds, and transfers of remaining balances when funds are closed are classified non-operating revenue.
4. Loans/Advances - Loans between funds are classified as interfund loans receivable and payable or as advances to and from other funds in the fund statements. Interfund loans do not affect total fund equity, but advances to other funds are offset by a reservation of fund equity. Loans and Advances are subject to elimination upon consolidation.

B. Interfund Receivables and Payables

The following table depicts interfund receivable and payable balances as of December 31, 2004:

| <i>Fund Types</i> | Due to Other Funds | Due From Other Funds |
|------------------------------|---------------------------|-----------------------------|
| General Fund | \$ 173,335 | \$ 248,205 |
| Roads | 483,945 | 20,838 |
| 2003 Construction Fund | 1,322 | - |
| Nonmajor governmental funds | 167,031 | 32,657 |
| Business-type Funds | | |
| SW Disposal District | 120,276 | 4,008 |
| Nonmajor business-type funds | 79,217 | 719,418 |
| TOTAL | \$ 1,025,126 | \$ 1,025,126 |

C. Interfund Loans

The following table displays interfund loan activity during 2004:

| <i>Interfund Loans</i> | | | | | |
|------------------------|---------------------|-------------------------|------------------|----------------------|-------------------------|
| Borrowing Fund | Lending Fund | Balance 01/01/04 | New Loans | Payments Made | Balance 12/31/04 |
| South County Airport | General | \$ 9,000 | \$ - | \$ - | \$ 9,000 |
| Community Development | ER&R | 20,639 | - | 20,639 | - |
| Flood Control Zone | Roads | 156,066 | - | 156,066 | - |
| TOTAL | | \$ 185,705 | \$ - | \$ 176,705 | \$ 9,000 |

D. Interfund Transfers

The following table displays interfund operating transfers during 2004:

| <i>Operating Transfers</i> | | |
|------------------------------|---------------------|---------------------|
| <i>Fund Types</i> | IN | OUT |
| General Fund | \$ 580,297 | \$ 2,701,210 |
| Roads | 27,328 | 27,383 |
| 2003 Construction Fund | 1,850,000 | |
| Capital Facilities Plan | 141,992 | 3,392,113 |
| Nonmajor governmental funds | 3,882,103 | 624,774 |
| Nonmajor business-type funds | 613,760 | 350,000 |
| TOTAL | \$ 7,095,480 | \$ 7,095,480 |

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NOTE 14 - NET ASSETS

The government-wide and business type fund financial statements utilize a net asset presentation. Net assets are the difference between assets and liabilities. Net assets are categorized as investment in capital assets (net of related debt), restricted, and unrestricted.

- A. Investment in Capital Assets (net of related debt) is intended to reflect the portion of net assets which are associated with non-liquid, capital assets less outstanding capital asset related debt.

The net related debt is the debt less the outstanding liquid assets and any associated unamortized cost. Additionally, until the infrastructure assets are reported, infrastructure related debt would reduce the investment in other non-infrastructure capital assets.

- B. Restricted Assets are liquid assets (generated from revenues and not bond proceeds) which have third party (statutory, bond covenant, or granting agency) limitations on their use. The County would typically use restricted assets first, as appropriate opportunities arise, but reserve the right to selectively defer the use thereof to a future project or replacement equipment acquisition.

- C. Unrestricted Assets represent unrestricted liquid assets. The County's management may have plans or tentative commitments to expend resources for certain purposes in future periods. Further legal action will be required to authorize the actual expenses or expenditures.

NOTE 15 - OTHER DISCLOSURES

A. Changes to Funds

Reorganization of existing funds in 2004:

None

New funds established in 2004:

None

Existing funds dissolved in 2004

1999 Construction Fund

NOTE 16 - JOINT VENTURES/JOINTLY GOVERNED ORGANIZATIONS

Lewis County was jointly participating with the city of Centralia and the city of Chehalis in the Chehalis-Centralia Airport. The joint venture is organized under RCW 14.08.200. Chehalis-Centralia Airport was jointly governed by an appointed seven-member board of which Lewis County is a member. Currently three airport board members are appointed by Lewis County. Lewis County has a one-third equity interest in the Chehalis-Centralia Airport. The equity position of the airport was a negative \$312,518 as of December 31, 2004, primarily as result of ongoing capital development at the airport. The county and the two cities made no cash contributions to the airport during 2004. On August 24, 2004 by joint resolution of the cities of Centralia and Chehalis and Lewis County, the action authorized the removal of the City of Centralia from the Chehalis-Centralia airport joint operating agreement and the two positions on the governing board held by representatives of the city of Centralia were eliminated.

Financial statements for the Chehalis-Centralia Airport can be obtained from its administrator at Airport, PO Box 1344, Chehalis, WA 98532.

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NOTE 17 - SUBSEQUENT EVENTS

The county issued \$7,100,000 Limited Tax General Obligation Refunding Bonds, Series 2005, on May 16, 2005, to refund a portion of the county's Limited Tax General Obligation And Refunding Bonds, 1999.

The county is unaware of the occurrence of any other subsequent events that would be material to the County's financial statements for the year ending December 31, 2004.